Docket Nos. 98-0252/-335 (Consol.)
Staff Exhibit 4.0
Attachment 4.01

J. Marshall Request

Calculation of FAS 71 Impacts ($000)		1995	1996	1997	1998	1999
Balance Available for Return per Schedule C of Exhibit 7.0		272,005	295,445	376,980	416,275	541,031
FAS 71 Amortization, net of tax		65,103	65,103	65,103	65,103	65,103
Revised Balance Available for Return		337,108	360,548	442,083	481,378	606,134
Net Original Cost per Schedule C of Exhibit 7.0		2,883,393	2,805,027	2,644,841	2,990,052	2,824,498
Depreciation Reserve Adjustment		107,906	215,812	323,718	431,624	539,530
Deferred Tax Reserve Adjustment		(42,804)	(85,608)	(128,412)	(171,216)	(214,020)
Revised Net Original Cost		2,948,495	2,935,231	2,840,147	3,250,460	3,150,008
Total FAS 71	143,875					
Illinois Intrastate @ 75%	107,906					
State Tax @ 7.18%	7,748					
Balance for federal tax	100,159					
Federal tax @ 35%	35,056					
Increased balance available	65,103					

Docket Nos. 98-0252/-335 (Consol.)
Staff Exhibit 4.0
Attachment 4.02

AMERITECH ILLINOIS SFAS 71 IMPACTS
ALL TREATED AS EXTRAORDINARY ITEMS
($000)

INCREASE IN DEPRECIATION RESERVE		1,154,894
WRITTEN DOWN ASSETS:		
COMPENSATED ABSENCES	20,818	
• SHORTING	20,642	
UNAMORTIZED DEBT ISSUE EXPENSE	19,529	
UNPAID MEDICAL EXPENSES	10,725	
DEFERRED INCENTIVE PAY	5,362	
CAPITALIZED LEASES	1,194	
LEASEHOLD IMPROVEMENTS	1,034	
• LIFE LINE LINK-UP	928	
PREMIUM/DISCOUNT ON LONG TERM DEBT	(30)	80,202
TOTAL EXTRAORDINARY ITEM CHARGE		1,235,096
EXTRAORDINARY ITEM CREDIT FOR INCOME TAXES		(503,310)
NET SFAS 71 CHARGE TO NET INCOME		731,786
ASI DEFERRED LEASE LOSS		998
TOTAL AMERITECH ILLINOIS IMPACT		732,784

Docket Nos. 98-0252/-335 (Consol.)
Staff Exhibit 4.0
Attachment 4.03

DLH-023
1/3

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-K

☒ ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934 (*FEE REQUIRED*) .... *For the fiscal year ended December 31, 1994*

OR

☐ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934

Commission File Number 1-2222

ILLINOIS BELL TELEPHONE COMPANY

An Illinois Corporation

I.R.S. Employer No. *36-1253600*

225 West Randolph Street
Chicago, Illinois 60606
Telephone Number 312-727-9411

Securities registered pursuant to Section 12(b) of the Act:

Thirty-Five Year 7⅝% First Mortgage Bonds, Series K, due April 1, 2006
Thirty-One Year 7¼% Debentures, due March 15, 2024

Exchanges on which registered: New York Stock Exchange, Chicago Stock Exchange

Securities registered pursuant to Section 12(g) of the Act: None

THE REGISTRANT, A WHOLLY OWNED SUBSIDIARY OF AMERITECH CORPORATION, MEETS THE CONDITIONS SET FORTH IN GENERAL INSTRUCTIONS J(1)(a) AND (b) OF FORM 10-K AND IS THEREFORE FILING THIS FORM WITH REDUCED DISCLOSURE FORMAT PURSUANT TO GENERAL INSTRUCTION J(2).

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports) and (2) has been subject to such filing requirements for the past 90 days.

Yes ☒ No ☐

expense. These changes have been applied retroactively and were made to correspond to financial reporting for unregulated enterprises.

B. Discontinuation of Regulatory Accounting — FAS 71

On a regular basis management has evaluated the continued applicability of FAS 71. In the fourth quarter of 1994, having achieved price regulation and recognizing increased competition, the Company concluded that GAAP prescribed by FAS 71 was no longer appropriate. As a result of the discontinuation of applying FAS 71, the Company recorded a fourth-quarter extraordinary noncash after-tax charge of $728.6. The following table is a summary of the extraordinary charge.

	Pretax	After-Tax
Increase to the accumulated depreciation balance	$1,151.5	$693.9
Elimination of other net regulatory assets	82.1	49.4
Tax-related net regulatory liabilities	—	5.5
Accelerated amortization of tax credits	—	(20.2)
	$1,233.6	$728.6

The adjustment of $1,151.5 to net property, plant and equipment was necessary since estimated useful lives and depreciation methods historically prescribed by regulators did not keep up with the rapid pace of technological changes in the Company and differed significantly from those used by unregulated enterprises. Plant balances were adjusted by increasing the accumulated depreciation balance. The increase to the accumulated depreciation balance was determined by a discounted cash flow analysis which considered technological changes, capital requirements and estimated impacts of future competition. To corroborate this study, a depreciation reserve study was also performed that identified inadequate accumulated depreciation levels by individual asset categories. The Company believes these levels developed over the years as a result of the systematic underdepreciation of assets resulting from the regulatory process. When adjusting its net property, plant and equipment, the Company gave effect to shorter, more economically realistic lives.

The discontinuance of FAS 71 also required the Company to eliminate from its consolidated balance sheet, prepared for financial reporting purposes, the effects of any actions of regulators that had been recognized as assets and liabilities pursuant to FAS 71, but would not have been recognized as assets and liabilities by enterprises in general. The elimination of other net regulatory assets primarily related to certain deferred vacation pay, debt financing costs, and certain deferred assets being reduced under regulatory principles, as well as certain other costs deferred and recognized as expense in accounting periods other than those required under GAAP, absent FAS 71.

The tax-related adjustments were required to adjust excess deferred tax levels to the currently enacted statutory rates and to eliminate tax-related regulatory assets and liabilities. Prior to the discontinuance of FAS 71, the Company had recorded deferred income taxes on the cumulative amount of tax benefits previously flowed through to ratepayers and recorded a regulatory asset for the same amount ($160.5 at December 31, 1993). Also the Company had recorded a regulatory liability for the difference between deferred taxes recorded at higher historical tax rates compared with those currently enacted and deferred taxes provided on unamortized investment tax credits ($227.9 at December 31, 1993). These regulatory assets and liabilities were grossed up for the tax effect anticipated when collected in future rates.

At the time the Company discontinued the application of FAS 71, the above tax-related regulatory assets and liabilities were eliminated and deferred tax balances adjusted to reflect application of FAS 109 consistent with other unregulated enterprises.

The Company uses the deferral method of accounting for investment tax credits and amortizes the credits as a reduction to tax expense over the life of the asset that gave rise to the tax credit. As asset lives were shortened, the investment tax credits deemed already earned were credited to income ($20.2).

The effects on the Company's consolidated financial statements going forward without FAS 71 are discussed in Management's Discussion and Analysis of Results of Operations.

C. **Income Taxes**

The components of income tax expense follow:

	1994	1993	1992
Federal			
Current	$226.0	$176.1	$178.8
Deferred, net	(41.9)	17.0	19.7
Investment tax credits, net	(14.6)	(18.2)	(18.5)
Total	169.5	174.9	180.0
State and local			
Current	43.5	35.7	17.4
Deferred, net	(6.7)	10.3	4.0
Total	36.8	46.0	21.4
Total income tax expense	$206.3	$220.9	$201.4

Total income taxes paid were $290.2, $231.9 and $224.3 in 1994, 1993 and 1992, respectively.

The following is a reconciliation between the statutory federal income tax rate for each of the past three years and the Company's effective tax rate:

	1994	1993	1992
Statutory federal income tax rate	35.0%	35.0%	34.0%
State income taxes, net of federal benefit	4.5	4.7	2.3
Reduction in tax expense due to amortization of investment tax credits	(2.7)	(2.8)	(3.0)
Real estate write-down requiring valuation allowance	2.5	—	—
Effect of adjusting deferred income tax balances due to tax law changes	—	(1.4)	—
Benefit of tax rate differential applied under FAS 71 applied to reversing temporary differences	(1.3)	(1.8)	(2.2)
Other	0.7	0.9	1.7
Effective income tax rate	38.7%	34.6%	32.8%

The Revenue Reconciliation Act of 1993, enacted in August 1993, increased the statutory federal income tax rate for 1993 to 35%. In accordance with the liability method of accounting, the Company adjusted, on the enactment date, its deferred income tax balances. The result was a reduction in deferred income tax expense of $8.9 primarily from increasing the deferred tax assets associated with FAS 106 and 112 (see Note E).